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IN THE

Supreme Court of the United States

OCTOBER TERM, 1946.

No. 454

JOSEPH B. FLEMING and AARON COLNON, Trustees of THE CHICAGO, ROCK ISLAND AND PACIFIC RAILWAY COMPANY, *et al.*,

Petitioners,

vs.

JOHN C. TRAPHAGEN, JAMES E. GOWEN, GEORGE H. WILSON and CHARLES G. WOODWARD, constituting the Protective Committee for holders of Choctaw and Memphis Railroad Company First Mortgage 5% Gold Bonds, due January 1, 1949,

Respondents.

BRIEF IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI.

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Respondents.

BRIEF IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI.

Preliminary Statement.

This brief is submitted in behalf of John C. Traphagen and others as the Protective Committee for the Choctaw and Memphis 5% Gold Bonds (herein called the C&M COMMITTEE) in opposition to the petition for a writ of certiorari filed by the Trustees of The Chicago, Rock Island and Pacific Railway Company (herein called the DEBTOR PACIFIC COMPANY) to review an order and decree of the Circuit Court of Appeals for the Seventh Circuit entered June 17, 1946, reversing an order or decree of the District Court for the

Northern District of Illinois, Eastern Division, in the reorganization proceedings of the Debtor Pacific Company. The opinion of the Circuit Court (R., pp. 245-252) is reported in 155 F. (2d) 889. The opinion of the District Court (R., pp. 156-158) is not reported.

The issue in this case arose with respect to the Choctaw and Memphis First Mortgage 5% Gold Bonds (herein called the C&M Bonds) which upon final reorganization were found to be in so superior a position as to be unaffected by the reorganization Plan. These bonds are protected by a first mortgage lien on a division of the Debtor Pacific Company, including a perfected first mortgage lien on the income of the division. This income, after prior charges, is in excess of the amounts required for the interest on the bonds during the reorganization proceeding. However, the District Court withheld payment of such interest, for periods of upwards of eleven years in instances, because of the cash requirements of the railroad system as a whole and the insufficient earnings of other divisions of the railroad.

The question litigated below was whether the holders of these bonds, under the foregoing circumstances, were entitled to recover interest on the bond coupons from their respective dates of maturity until paid. The District Court disallowed the claim. The Circuit Court of Appeals reversed.

The petitioners in their statement of the matter involved have obscured the narrow issue and simulated others, principally through misplaced emphasis and omission. Since many of the issues sought to be raised are essentially factual, it must be stressed that the factual version of the case presented by petitioners is inadequate. A presentation of the more important facts upon which the Circuit Court of Appeals order is founded, therefore, is necessary.

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Statement of Facts.

The C&M Bonds were issued by Choctaw and Memphis Railroad Company in the principal amount of $3,524,000 under an Indenture (herein called the C&M Indenture) dated January 2, 1899 (R., pp. 61-88). These bonds constitute a first mortgage on 280 miles of railroad extending from the west bank of the Mississippi River opposite Memphis, Tennessee, to the Oklahoma-Arkansas line, on appurtenances to this line, on certain property in Memphis and on "all the rents, issues, tolls and income of said mortgaged railroad hereinbefore described" (R., pp. 66-68).

The Debtor Pacific Company owns all the capital stock of the successor of the mortgagor and, as stated by petitioners below, has never taken title to the mortgaged property "although it could have done so at any time after acquiring all the stock."

In the C&M Indenture, the mortgagor covenanted to pay interest on the bonds "at the times, at the rate, and in the manner mentioned therein, and the coupons thereto belonging, according to the true intent and meaning thereof" (R., p. 71). The coupons appurtenant to the bonds are negotiable in form and contain unconditional promises for payment by the mortgagor on specified semi-annual dates "at its office in the city of Philadelphia, or at its agency in the city of New York" (R., p. 65).

In addition, the C&M Indenture provides that in the event of default for three months in the payment of interest on the C&M Bonds, the trustee of the C&M Indenture may take possession of the mortgaged property and, among other things, "collect and receive all tolls, freights, incomes, rents, issues, and profits of the same, and every part thereof" (R., pp. 74-75). It further provides that such

trustee may, in lieu of taking possession, apply to a court for the appointment of a receiver to exercise such power under the C&M INDENTURE, and the mortgagor assents to the appointment of such receiver (R., pp. 75-76).

On May 2, 1934, the District Court entered its Sequestration Order in the reorganization proceedings of the DEBTOR PACIFIC COMPANY (R., pp. 20-22), in which it was provided (R., p. 21):

> "That no Trustee of a mortgage shall be required to make any further demand or application for the enforcement in this proceeding of any lien or right in respect of any of the tolls, earnings, incomes, rents, issues and profits of the property covered by the mortgage * * *; but the rights of each Mortgage Trustee shall be determined as if due demand or application had been made by such Trustee * * * at the earliest date or dates when any such Trustee would have been entitled to make such demand or application under the terms of the mortgage of which it is Trustee * * *."

The Sequestration Order also provided (R., pp. 21-22):

> "That the respective Trustees of the mortgages shall be entitled to apply at the conclusion of this proceeding, or at such earlier time or times as they may respectively deem proper, upon due notice to all parties of record, for the enforcement of their liens upon, or rights in, the tolls, earnings, incomes, rents, issues and profits in which they may have any interest, and of their liens upon, or rights in, any of the proceeds thereof, and for an equitable adjustment, as between those interested in this proceeding, with respect to any use which may have been made of any of the same; but nothing in this order shall be construed as determining the merits of any such application or as requiring the Trustees to pay over or earmark any of the same pending the further order of the Court."

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Pursuant to the Sequestration Order, formulas were devised for the allocation of earnings reflecting the interests of the various mortgages (R., pp. 28-30). The District Court authorized the discontinuance of the segregation of earnings after one of the formulas had been applied for the period of from June, 1933, to May, 1934, inclusive, because of the labor and expense involved (R., pp. 30-31). The applications of the formula for that twelve-month period showed, however, that the earnings available for interest on the C&M Bonds, after providing for all taxes and prior charges, amounted to $389,884. The interest requirements on the C&M Bonds equal $176,200 per year. Although this first formula was not approved by the court nor accepted by the parties, it was applied by the Trustees, who had no axe to grind.

A second formula was approved by the District Court (R., pp. 49-51) and applied to the earnings of the Denver Pacific Company for the year 1936 and, as adjusted, to the year of 1937 (R., pp. 56-57). These approved formulas became the principal basis adopted by the Interstate Commerce Commission for allocations to security holders under the Plan. The results of applying these formulas show adjusted income of $450,882 available for interest on the C&M Bonds in 1936 and $399,304 so available in 1937, as contrasted with annual interest requirements on the C&M Bonds of $176,200 (252 I. C. C. 483, 488-493).*

The most important point regarding the earnings coverage of the C&M Bond interest—and the point overlooked by the petitioners (petition, pp. 21-23)—is that the Interstate Commerce Commission has expressly found that (R., p. 128):

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* This report is part of the record but, pursuant to stipulation of the parties, has not been printed (R., pp. 233-236).

> "The Choctaw & Memphis is a leased line, and the record establishes the fact that its earnings are substantially in excess of its bond interest requirements."

Repeatedly during the twelve years in which the reorganization has been pending, respondents petitioned the District Court to allow to them their interest as it matured, and, after maturity of the coupons, interest on their coupons (R., pp. 39-44, 104-110, 124-125, 130-135, 198-211). The coupons which matured July 1, 1933, and January 1, 1934, were ordered to be paid on June 26, 1933, and January 29, 1935, respectively (R., pp. 8-9, 32-36). The span of years from 1935 to 1945 witnessed no payment of interest.

After numerous preliminaries, the District Court on May 14, 1945, approved the Plan of Reorganization subject to certain corrections and clarifications. The C&M Bonds alone of all the securities issued by the entire Rock Island system were held to occupy such a superior position as to be unaffected by the Plan. The decree approving the Plan provides that as approved it shall contain the following provision (R., p. 194):

> "The Choctaw & Memphis Railroad Company first mortgage dated January 2, 1899, and the $3,524,000 of 5-per cent bonds issued thereunder and outstanding in the hands of the public shall remain undisturbed and unaffected by the plan, with preservation of lien and rights of bondholders as set forth in said mortgage and said bonds. For the $1,762,000 of unpaid accrued interest to January 1, 1944, the holders of the bonds shall receive cash, as hereinafter stated."

The Plan, as it had been certified by the Commission to the court, provided that the question of whether interest should be allowed on the unpaid matured coupons of the

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C&M Bonds should be determined by the court (R., p. 128). On May 11, 1945, the District Court denied interest on these coupons (R., pp. 156-158).

Respondents appealed from this denial (R., pp. 174-175). The Circuit Court of Appeals unanimously reversed the judgment of the District Court, holding that it was in error to refuse to order the payment of simple interest on the coupons after their respective dates of maturity until the date of payment (R., pp. 245-252).

ARGUMENT.

POINT I.

Whether the C&M Bonds are within or without the Plan does not affect the rights of the holders to recover interest on matured coupons, and therefore it would be pointless for this Court to grant petitioners' request for a review of that issue.

Petitioners' brief, pages 17 to 20, devotes considerable argument to their contention that the C&M Bonds are still a part of the Plan and the reorganization proceedings. It is asserted that the statutory power conferred by Section 77 of the Bankruptcy Act requires that the satisfaction of all claims must emanate from a reorganization plan. Assuming *arguendo* that this is true, it does not affect the recovery by the C&M bondholders of interest on overdue coupons.

The Circuit Court of Appeals proceeded on the basis of the findings and judgment of the District Court, and held that the bonds were "no part of the reorganization, in no wise affected by it, and, so far as rights and remedies are concerned, occupy the same position they would have had there been no bankruptcy" (R., p. 246). Under this theory the doctrine of *Erie Railroad Co.* v. *Tompkins,* 304 U. S. 64

(1938), governed the case. As will be pointed out *infra*, Pennsylvania law would then apply and the bondholders would be entitled to the interest.

If, on the other hand, we accept the position of the petitioners that the rights of the C&M bondholders emanate from the Plan, then, on their theory, *Prudence Corp.* v. *Geist*, 316 U. S. 89 (1942), is applicable. This would require the application of federal law which, as will be pointed out *infra*, does not differ from that of Pennsylvania but also allows recovery on matured coupons.

It would therefore affect no substantial rights for this Court to answer the question, sought to be raised by the petitioners, as to the meaning of the words in the District Court plan decree: "undisturbed and unaffected by the plan."

POINT II.

On the question of the bondholders' right to be paid interest on their matured coupons, the court below followed the Pennsylvania law, which is in conformity with the federal decisions, and therefore no substantial result would be accomplished by this Court if it reviewed the question of which law to apply.

The decision of the Circuit Court of Appeals proceeds on the theory that the C&M bondholders, being adequately secured, protected by impounded income greatly in excess of interest requirements and expressly excluded from the operation of the Plan, are entitled to have their rights determined as if there were no bankruptcy proceeding. The court then held that, under the doctrine of *Erie Railroad Co.* v. *Tompkins*, 304 U. S. 64 (1938), state law should be applied. The coupons are payable in Philadelphia (R., p. 63). Under

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the law of Pennsylvania, the coupons, as negotiable instruments, bear interest from the date of payment.

County of Beaver v. *Armstrong,* 44 Pa. St. (8 Wright) 63 (1862);
Williamsport Gas Co. v. *Pinkerton,* 95 Pa. 62 (1880);
Philadelphia & R. R. Co. v. *Knight,* 124 Pa. 58, 16 Atl. 492 (1889);
Appeal of Cadwalader et al., 249 Pa. 239, 94 Atl. 833 (1915);
McDowell v. *North Side Bridge Co.,* 251 Pa. 585, 97 Atl. 97 (1916).

That the law of Pennsylvania allows interest on overdue coupons has not been contested by the petitioners at any time.

The contention of the petitioners is that under the doctrine of *Prudence Corp.* v. *Geist,* 316 U. S. 89 (1942), the court should have applied federal law. The application of federal law, however, would not help the petitioners. As we pointed out below, and as the opinion of the Circuit Court of Appeals notes (R., p. 250), the federal decisions are in accord with the Pennsylvania law and hold that interest coupons draw interest from their dates of maturity.

Gelpcke v. *The City of Dubuque,* 1 Wall. 175 (1863);
Aurora City v. *West,* 7 Wall. 82 (1868);
Town of Genoa v. *Woodruff et al.,* 92 U. S. 502 (1875);
Cromwell v. *County of Sac,* 96 U. S. 51 (1877);
Brine v. *Insurance Co.,* 96 U. S. 627 (1877);
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Edwards v. *Bates County*, 163 U. S. 269, 272 (1896);

Roswell Drainage Dist. v. *Parker*, 53 F. (2d) 793, 797 (C. C. A. 10th, 1931);

Sears v. *Greater New York Development Co.*, 51 F. (2d) 46, 49 (C. C. A. 1st, 1931), *cert. denied*, 284 U. S. 668 (1931).

The petitioners attempt to distinguish these cases on the basis that they do not involve bankruptcy proceedings. However, they cannot cite any cases involving bankruptcy proceedings which change the law or which disclose law in favor of their contentions. The decisions are that bankruptcy does not affect the enforceability of a claim for interest if the assets on which the claim is a first lien are adequate to pay interest.

Coder v. *Arts*, 213 U. S. 223, 245 (1909);

American Iron and Steel Manufacturing Co. v. *Seaboard Airline Railway*, 233 U. S. 261, 266-7 (1914);

Board of Commissioners of Sweetwater County v. *Bernardin*, 74 F. (2d) 809, 815 (C. C. A. 10th, 1934), *cert. denied*, 295 U. S. 731 (1935).

Indeed, this much is expressly admitted by the petitioners (brief, p. 26).

Moreover, in an ordinary bankruptcy proceeding, if a claim is secured by collateral which realizes earnings after the date of the filing of the petition, such earnings must be applied to interest accruing on the claim after the filing of the petition.

Sexton v. *Dreyfus*, 219 U. S. 339, 346 (1911).

See, also, the opinion of the court below (R., p. 248).

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It would therefore be profitless so far as the present case is concerned for this Court to review the question of whether state law or federal law applies, since the substantial result of the case would not be affected. The same thing cannot be said of *In re American Fuel & Power Co.*, 151 F. (2d) 470 (C. C. A. 6th, 1945), in which certiorari was granted on March 25, 1946, *sub nom. Vanston Bondholders Protective Committee* v. *Green*, 66 S. Ct. 822. In that case, the Circuit Court of Appeals followed the unusual New York rule and disallowed simple interest on overdue coupons. The opinion recognizes, however, that the federal rule is to the contrary. A review of that case by this Court may, therefore, change the effect of that decision upon the rights of the parties.

The petitioners point out that the mortgage does not specifically mention a lien for interest upon matured coupons. They further assert that by its terms the C&M INDENTURE "affirmatively" shows that there was no intention to pay interest on overdue coupons and that the claim for interest on overdue coupons is "expressly given up." This contention overlooks the fact that the mortgage, the bonds and the coupons do "expressly" provide that the coupons were to be paid on their respective maturity dates.

If any "affirmative" proposition is to be derived from the provision of the relevant documents, it is that the coupon holders were deprived of their rights when they did not receive payment on the coupons as they matured, particularly when there was a perfected lien on earnings available for the payment of such interest. The C&M INDENTURE of 1899 sets forth remedies which were then well recognized in railroad mortgages. It contemplates that those remedies may be exercised promptly. The draftsman of the C&M INDENTURE obviously did not have in mind any situation in which the interest on the C&M BONDS would remain in de-

fault for almost twelve years despite the fact that earnings of the mortgage property were adequate to pay the interest. It is absurd to impute to the draftsman of the mortgage an intent to give up interest on the overdue coupons in the situation here presented. As the Circuit Court of Appeals stated (R., p. 251):

> "But we have seen that the indenture pledges the property to secure the payment of principal and interest according to 'the true tenor' of the bonds and interest and that the true tenor of the coupons, properly interpreted, includes a legal obligation to pay interest after maturity. It follows that, by necessary implication, the mortgage creates and preserves a lien for the bonds, coupons and simple interest on the coupons after maturity."

The petitioners in their brief in support of their petition for certiorari (pp. 21-23) for the first time seek to raise the question of whether the earnings of the mortgaged property were adequate to cover the bond interest requirements, and they present the issue as if this Court should take on the labor of re-examining and re-applying the formulas on which the Interstate Commerce Commission based its findings. The petitioners misconceive the function of this Court in reviewing cases on appeal. The Interstate Commerce Commission expressly found that "the record establishes the fact that its earnings [*i.e.*, those of the Choctaw & Memphis mortgage division] are substantially in excess of its bond interest requirements" (R., p. 128). That finding cannot be questioned for the first time in this Court.

It is argued that if interest be allowed on the overdue C&M coupons there are other bonds in the estate of the Debtor Pacific Company which likewise are entitled to interest on overdue coupons. The record is wholly lacking

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in facts on which the Court could make a determination of that question. That the respondents' assertion in this regard is without foundation may be inferred, however, from the fact that the C&M Bonds alone of all the security issues in the estate of the Debtor Pacific Company are in so superior a position as not to be affected by the Plan.

Conclusion.

The petition for a writ of certiorari should be denied.

September 23, 1946.

Respectfully submitted,

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PETITION OF JOHN C. TRAPHAGEN AND OTHERS FOR HEARING AND ARGUMENT.

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PETITION OF JOHN C. TRAPHAGEN AND OTHERS FOR HEARING AND ARGUMENT.

This is an application for reconsideration of, and for permission to submit briefs and to argue, a case in which certiorari has been granted and which has then been reversed by this Court without benefit of either briefs or argument (*per curiam* decision handed down December 16, 1946, not yet reported).

The decision which has thus been summarily reversed was the unanimous decision of the Circuit Court of Appeals for the Seventh Circuit (R., p. 245; 155 F. [2d] 889).

That decision was made in the first case to reach this Court, under either Section 77 or Chapter 10 of the Bankruptcy Act, involving the rights of security holders who

have been found to be in so superior a position as to be unaffected by the plan of reorganization. The Choctaw & Memphis Bonds which are here involved have been expressly found to be in that position (R., p. 194).

This case is also only the second case to reach this Court on the question of the allowance of simple interest on overdue bond coupons in a bankruptcy or other reorganization.*

It is the first case to reach this Court on the question of the allowance of such interest in such a proceeding where, during the time when the coupons matured, they were protected by a lien, duly perfected by a sequestration order (R., p. 21), on earnings substantially in excess of the coupon requirements.

This case was reversed *per curiam* on the authority of *Vanston Bondholders Protective Committee* v. *Green*, decided December 9th, Nos. 42 to 45, October Term, 1946.

Under the *Vanston* case, the question of whether simple interest on overdue coupons should be allowed is a question to be determined by the bankruptcy court sitting as a court of equity. In that light the *Vanston* case was decided on its own unique facts: "under the circumstances shown by this case" (slip sheet opinion, pp. 5-6). Moreover, the *Vanston* case holds that "the touchstone of *each decision* on allowance of interest in bankruptcy, receivership and reorganization has been a balance of equities

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* This Court's decisions where bankruptcy or reorganizations were not involved, however, have universally allowed such interest contrary to the *per curiam* decision in the instant case. *Gelpcke et al.* v. *The City of Dubuque*, 1 Wall. 175 (1863); *Aurora City* v. *West*, 7 Wall. 82 (1868); *Town of Genoa* v. *Woodruff et al.*, 92 U. S. 502 (1875); *Cromwell* v. *County of Sac*, 96 U. S. 51 (1877); *Brine* v. *Insurance Co.*, 96 U. S. 627 (1877); *Amy* v. *Dubuque*, 98 U. S. 470 (1878); *Koshkonong* v. *Burton*, 104 U. S. 668, 676-7 (1881); *Edwards* v. *Bates County*, 163 U. S. 269, 272 (1896); *Sears* v. *Greater New York Development Co.*, 51 F. (2d) 46, 49 (C. C. A. 1st, 1931), *cert. denied*, 284 U. S. 668 (1931).

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between creditor and creditor or between creditors and the debtor" (*ibid.* p. 7; emphasis added).

The question which is made the test in the *Vanston* decision—namely, the equities arising from the circumstances shown by each particular case—was expressly reserved in the instant case, when the sequestration order provided that the trustees of the respective mortgages should be entitled, at the conclusion of the proceeding, to apply for the enforcement of their liens upon tolls, earnings, profits, etc., "and for an equitable adjustment, as between those interested in this proceeding, with respect to any use which may have been made of any of the same * * *" (R., pp. 21-22).

This Court has never had opportunity to consider the circumstances which exist in the instant case and out of which strong equities in favor of the Choctaw & Memphis bondholders arise.

The circumstances in the instant case materially distinguishing it from the *Vanston* case are as follows:

1. As stated above, the bonds in the instant case have been ordered to "remain undisturbed and unaffected by the plan, with preservation of lien and rights of bondholders as set forth in said mortgage and said bonds" (R., p. 194). This order results from the provisions in Section 77 which put a security outside the scope and purposes of that section when it is so imperviously secured as to be undisturbed by the bankruptcy turbulence affecting all its juniors. As the court below stated (R., pp. 247-48):

> "But this power to deal with or modify securities, we think, in no way affects appellants [*i.e.*, Choctaw & Memphis bondholders] who are no part of the reorganization but constitute secured holders of instruments wholly unaffected thereby. Hence it is

> improper to say that the bankruptcy court had the power to alter their securities. Indeed, quite the contrary is true, for, in their preferred situation, they hold securities wholly outside the reorganization."

Only through the plan can creditors' rights be permanently affected and readjusted. But it is a travesty to say that a security is unaffected if no compensation is allowed for the withholding of its interest for as much as eleven years. Only by ignoring actuality can one say that the right to receive money today can be turned into a right to receive money eleven years from now without affecting the value of that right.

Indeed, this Court has recognized the realities of such an extension of maturity date. In *Consolidated Rock Products Co.* v. *Du Bois*, 312 U. S. 510, 527-28 (1941), immediately preceding the often quoted language that "full compensatory provision must be made for the entire bundle of rights" of a creditor, the opinion discusses the fact that the bondholders in that case had not been "made whole" because, among other reasons, their maturities had been in part extended, and the maturities thus extended were referred to as "lost rights" which were "of value." Except for tax purposes, the value of the right to receive money on a given date does not have any relationship to the question of whether the money is being paid and received by way of principal or by way of interest.

A creditor cannot, therefore, be said to be unaffected if the maturity date of an obligation of the debtor to pay money to him is materially extended.

2. In this case, the Choctaw & Memphis Bonds had a perfected lien on earnings substantially in excess of the bond interest requirements, and these earnings were pro-

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duced by the property covered by the Choctaw & Memphis mortgage. In the words of the Circuit Court of Appeals, "the annual earnings properly allocable to the division upon which they are a lien exceeds substantially the interest requirements" (R., p. 246). But for the hand of the bankruptcy court which, for the benefit of the junior interests, stayed the payment of the interest coupons as they matured, the Choctaw & Memphis Bonds had an enforceable right to receive, out of such earnings, payment of the coupons on their maturity dates.

Although the earnings subject to the lien of the Choctaw & Memphis mortgage were not segregated, they were a part of the cash in the hands of the Trustees of the Debtor and should have been dealt with in the light of the fact that there was a first mortgage lien on those earnings for the protection of debts which had not been paid when due. And by debts, the interest coupons are referred to and not the bonds themselves; for interest coupons, being promises to pay certain sums on definite due dates, are commercial paper in their own right, as has been often held by this and other courts.*

3. The bonds which are here involved were originally issued when Choctaw & Memphis Railroad, which is the best earning division of the Rock Island line, was a separate and independent railroad. Choctaw & Memphis, by successive leases and consolidations, has become a part of the Rock Island system without any acquiescence on the part of the holders of the Choctaw & Memphis Bonds. This, however, is no cause for complaint if the senior position of the Choctaw & Memphis Bonds with respect to their mortgage division is not to be impaired.

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* See, for example, the cases cited, *supra*, footnote, page 2.

It is not contended that the court, having the task of operating this railroad system pending reorganization, is without power to take funds on which A has a perfected lien, in order to operate the less prosperous properties on which B has a lien or claim. But it is most strenuously urged that when the delay in reorganizing the properties and putting them back in the hands of owner-operators arises from disputes and controversies between parties junior to A, then it is most inequitable for the court, in order to operate the properties pending determination of those disputes and controversies, to borrow funds on which A has a perfected first lien without compensating A for such borrowing.

4. In this case, the Interstate Commerce Commission, in approving the plan as it was certified to the District Court, provided for extending for twenty years the maturity date of the Choctaw & Memphis Bonds and lowering their interest rate from 5% to 4% (R., pp. 164-5). It was thereafter that the bonds were found to be in so superior a position as to be unaffected by the plan (R., p. 189 at 193-4). However, the Commission's order on the plan as certified by it provided that the Choctaw & Memphis Bonds were to receive interest on overdue coupons if the court should determine as a legal matter that they are entitled to it (R., pp. 128, 164). The Interstate Commerce Commission, as the expert body charged by Congress with formulating plans, was therefore of the opinion, as a matter of equity—since its task is to formulate a *fair* and *equitable* plan—that the Choctaw & Memphis Bonds should have their right to interest on overdue coupons recognized if such right legally exists. Clearly that right does exist under the law of Pennsylvania, which, aside from the doctrine of the *Vanston* case, nobody has disputed is the applicable law with respect to these coupons.

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Williamsport Gas Co. v. *Pinkerton*, 95 Pa. 62 (1880);
Appeal of Cadwalader et al., 249 Pa. 239, 94 Atl. 833 (1915);
McDowell v. *North Side Bridge Co.*, 251 Pa. 585, 97 Atl. 97 (1916).
See also opinion below, R., p. 245 at 250.

What, then, are the equities which would move the bankruptcy court, sitting as a court of equity, to strike down this well recognized right? Equities arise out of facts, and whether a particular equity has its basis in reality or in imagination can be determined only from factual analysis and experience. It is therefore of significance that the Interstate Commerce Commission felt as it did. It is likewise of significance that the Securities and Exchange Commission, with its vast experience in reorganizations under Section 11 of the Public Utility Holding Company Act and as adviser to the courts under Chapter 10 of the Bankruptcy Act, should feel that interest on overdue coupons should be allowed.* If the test is a test of whether or not it would be equitable to allow simple interest on overdue coupons, that test can be applied only through a careful sifting of the record to determine where the equities lie in a particular case.

5. When the habit of defaulting on the Choctaw & Memphis bond interest was formed in the early days of this reorganization proceeding, the only alternative to borrowing money from the funds on which those bonds had a per-

* See *Matter of Childs Company, Debtor*, SEC Corporate Reorganization Release No. 67 (1946), pp. 39-40; same case, SEC Corporate Reorganization Release No. 69; same case, CCH Bankruptcy Law Service, par. 55,779 (U. S. D. C., S. D. N. Y., 1946); see, also, brief of Securities and Exchange Commission in *Vanston* case.

fected lien was to borrow additional money from outsiders. Clearly, such a borrowing on trustees' certificates would have borne interest, as is illustrated by the trustees' certificates which in fact were issued in this case.

It cannot be said that a court can take A's money and lend it to B interest free merely because the court already has A's money in its custody. The custody over the fund does give the court, as a court of equity, authority to compel the loan, but only on terms which in equity recognize the full rights of A. In other words, the court had custody of the impounded funds of the Choctaw & Memphis division which were available for the payment of the Choctaw & Memphis interest coupons as they matured and which, but for the court's intervention, would have been paid on the Choctaw & Memphis coupons as they matured. Therefore, when the court deprived the holders of those coupons of their interest moneys on the due dates, it could do so in equity only by compensating the holders for such deprivation of substantial and valuable rights.* Any other holding is not equitable. It is not even well directed charity; for the senior securities in railroad reorganizations are for the most part held by insurance companies and fiduciaries whose *cestuis* are dependent upon them, whereas junior securities by and large are more apt to be held by persons who are willing and able to speculate.

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* It is suggested that if this Court, after considering the instant case on the basis of briefs and argument, should feel that the legal right to interest under the Pennsylvania law must be stricken down under some bankruptcy doctrine, nevertheless under the doctrine of the *Vanston* case, the bankruptcy court, as a court of equity, should compensate the Choctaw & Memphis bondholders for the use of their funds by the payment of interest, not at the legal rate in Pennsylvania, but at the prevailing rates existing from time to time as the funds subject to the lien of the Choctaw & Memphis mortgage were borrowed—*i.e.*, at the rate or rates which the Trustees of the Debtor would otherwise have had to pay.

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6. The instant case presents squarely to the Court the issue which is reserved in the concurring opinion of Mr. Justice Frankfurter in the *Vanston* case. That opinion shows that under the law of New York, where the *Vanston* coupons were payable, interest on overdue coupons is not allowed. There was, therefore, no legal right which the bankruptcy court had to consider. Here we have bond coupons which are clearly governed by the law of Pennsylvania. No one has disputed that. Under the law of Pennsylvania, these bond coupons have a legal right to interest if they are not paid on their due dates. (See cases cited *supra*, p. 7.) That right is *not* a penalty. The Pennsylvania cases are clear that the right arises from the fact that a bond coupon is independent commercial paper, passing in the market as a negotiable instrument, and therefore, like such instrument, bearing interest from its maturity date if not paid.

A secured debt other than a coupon has always borne interest even in a bankruptcy or reorganization proceeding if the security was adequate,* or if the earnings of the property securing the debt were adequate for the payment of interest.† Therefore, the question is squarely presented whether Congress in the Bankruptcy Act has enunciated any doctrine which prevents the recognition of what is in this case a clear legal right—an issue which was not really before the Court in the *Vanston* case in view of the New York law as pointed out in the decision by Mr. Justice Frankfurter.

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* *Coder* v. *Arts*, 213 U. S. 223, 245 (1909); *American Iron and Steel Manufacturing Co.* v. *Seaboard Airline Railway*, 233 U. S. 261, 266-7 (1914); *Consolidated Rock Products Co.* v. *Du Bois*, 312 U. S. 510, 527 (1941); *Group of Institutional Investors* v. *Chicago, Milwaukee, St. Paul & Pacific Railroad Company*, 318 U. S. 523, 546 (1943).

† *Sexton* v. *Dreyfus*, 219 U. S. 339, 346 (1911).

In view of the fact that there has been no hearing in this case, this is not an application for a rehearing. However, by analogy to the procedure prescribed by Rule 33 of this Court, counsel hereby certifies that this petition is presented in good faith and not for delay.

In view of all the foregoing considerations, this Court is respectfully urged to reconsider its *per curiam* decision of December 16, 1946, and in connection with such reconsideration to permit the filing of briefs and the presentation of oral argument on the issues involved in this case.

January 2, 1947.

Respectfully submitted,

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